

Internal Revenue Service

memorandum

CC:TL-N-83-90

TS/LJBYUN

date: DEC 4 1989

to: District Counsel, Thousand Oaks W:TO
Attn: Bradley D. Magee

from: Senior Technician Reviewer
Tax Shelter Branch CC:TL:TS

subject: [REDACTED]

This is in response to your request for tax litigation advice regarding a Scar issue in the above-mentioned case. It is our understanding that the taxpayers did not file a petition in the Tax Court and have not yet filed a complaint in the District Court or Claims Court. If a complaint is filed in the District or Claims Court, the case would be appealable to the Ninth Circuit.

ISSUE

Is the statutory notice of deficiency in this case valid under Scar v. Commissioner, 814 F.2d 1363 (9th Cir. 1987)?

CONCLUSION

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FACTS

A statutory notice of deficiency was issued to the [REDACTED] on [REDACTED], for the taxable year [REDACTED].¹ The deficiency

¹ You indicate that the deficiency notice was return unclaimed. Presumably the taxpayers secured a copy of the deficiency notice in [REDACTED] since the taxpayers make the following comment in their first amended return:

This collection activity was pursued while the Revenue Officers were attempting to obtain a copy of the Statutory Notice of Deficiency, which had not been received by the taxpayers. Such copy was finally

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notice specified a deficiency in the amount of \$ [REDACTED] arising from disallowed losses in the amount of \$ [REDACTED] with respect to [REDACTED]. The deficiency notice used the "smoking gun language" of Scar ("In order to protect the government's interest and since your original income tax return is unavailable at this time, the income tax is being assessed at the maximum tax rate of [REDACTED]%".)

The [REDACTED]'s [REDACTED] federal income tax return confirms that the right tax shelter and right amount was reflected on the deficiency notice since the [REDACTED] did claim \$ [REDACTED] of losses attributable to [REDACTED].² You surmise that the Service may have learned of the [REDACTED] investment in [REDACTED] from a Schedule K-1.

It is unclear whether a transcript of account was available and/or used at the time the deficiency notice was prepared. We note that the transcript of account which was attached to the tax litigation advice request reflects a cycle of [REDACTED] (i.e., week of [REDACTED]). Accordingly, this transcript of account was secured after the deficiency notice was issued (i.e., [REDACTED]) and there is no indication that an earlier transcript of account was requested and/or used.

Because the 90-day period under section 6213(a) has elapsed, the taxpayers cannot file a petition in the Tax Court. However, the taxpayers may still be able to file a complaint in either the District or Claims Court since it appears that the Service has not yet formally disallowed the taxpayers' claim for refund made on their first Form 1040X.

DISCUSSION & CONCLUSION

The Ninth Circuit Court of Appeals held in Scar v. Commissioner, 814 F.2d 1363 (9th Cir. 1987), revq. 81 T.C. 855 (1983), that the deficiency notice issued by the Service was

obtained by the Service on [REDACTED], two months after the Service completed collection for [REDACTED].

² We note that two amended returns were also filed with respect to the [REDACTED] year. The first Form 1040X was received by the Service on [REDACTED], and it claims a refund of \$ [REDACTED] (the amount of the deficiency asserted). It alleges that the deficiency was collected by the Service in [REDACTED]. The second Form 1040X was received by the Service on [REDACTED]. This form expressly states that it is a protective claim for refund, and that the amount of the refund will "be determined by the eventual outcome of the Heitzman appeal and any subsequent [REDACTED] test case litigation."

invalid since the Service had not made a "determination" of the taxpayers' correct tax liability. In coming to this conclusion, the Ninth Circuit stated that the "determination" requirement of section 6212(a) has "substantive content." According to the Ninth Circuit, a "determination" implies that the taxpayer's return has been examined where one has been filed. In other words, the "Commissioner must consider information that relates to a particular taxpayer before it can be said that the Commissioner has 'determined' a 'deficiency' in respect to that taxpayer." Id. at 1368.

In Scar, the Service did not have the taxpayers' return at the time the deficiency notice was being prepared. In addition, the wrong tax shelter was referred to in the notice and the deficiency was backed into by simply multiplying the adjustment by the maximum rate. Moreover, the deficiency notice specifically admitted that the return had not been examined and that the maximum rate was being applied (i.e., the "smoking gun language" was used). Based on these facts, the Ninth Circuit came to the following conclusion:

Because the Commissioner's purported notice of deficiency revealed on its face that no determination of tax deficiency had been made in respect to the Scars for the 1978 tax year, it did not meet the requirements of section 6212(a). Scar v. Commissioner, 814 F.2d at 1370.

In Clapp v. Commissioner, 875 F.2d 1396 (9th Cir. 1989), the Ninth Circuit limited the scope of Scar by clarifying that only where the deficiency notice is incorrect on its face is the Commissioner required to prove that a determination was made. The Court stated: "Furthermore, as the Tax Court has since pointed out, Scar did not even require any affirmative showing by the Commissioner that a determination set forth in an alleged notice of deficiency was made on the basis of the taxpayers' return. Only where the notice of deficiency reveals on its face that the Commissioner failed to make a determination is the Commissioner required to prove that he did in fact make a determination. Campbell v. Commissioner, 90 T.C. 110 (1988). Here, nothing on the face of the notice reveals that the Commissioner failed to make a determination." Clapp v. Commissioner, 875 F.2d at 1402. (Emphasis added).

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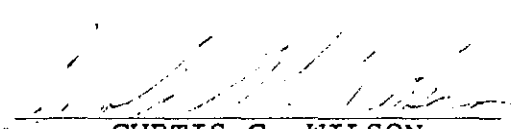
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For the reasons stated above, we do not recommend defending this case. Should you have any further questions regarding this matter, please call Lisa Byun at FTS 566-3289.


CURTIS G. WILSON